CHAPTER – 10
INDIAN ECONOMY

INDIAN ECONOMI SYSTEM

After the freedom, leaders of independent India (like Jawaharlal Nehru) were confused with regard to economic system, to be followed in India.

- Some leaders were in favour of Socialist Economy. However, in a democratic country like India, complete dilution of private ownership was not possible (as was possible in case of the former Soviet Union).
- Capitalist Economy System did not appeal to Jawaharlal Nehru, our first Prime Minister, as under this system, there would be less chances for improvement in quality of life of majority of people.
- As a result, Mixed Economy (with best features of socialist and capitalist Economy) was adopted by the Indian Economy. In this view, India would be a socialist society, with a strong public sector, but also with private property and democracy.

ECONOMIC PLANNING

After adopting the 'Mixed Economic System', the next important step for the Government was to revive the poor, backward and stagnant economy, inherited from the British rule.

- For the development of Indian Economy, it was necessary for the Government to 'plan' for the economy, known as Economic Planning.
- Economic planning can be defined as making major economic decisions (what, how and for whom to produce) by the conscious decision of a determinate authority. On the basis of a Comprehensive survey of the economy as a whole.
- The Industrial Policy Resolution of 1948 and the Directive Principles of the Indian Constitution assigned a leading role to the public sector. Private sector was also encouraged to be part of the plan efforts.
- To make economic planning effective, the Government of India set up Planning Commission in 1950, under the chairmanship of the then Prime Minister pandit Jawaharlal Nehru.

- The purpose of the Commission was to carefully assess the human and physical resources of the country and to prepare the plans for the effective use of resources.
- The planning Commission fixed the planning period at five years, which began the era of 'Five Year Plans'.

Note: It must be noted that 'Planning Commission' is no more in existence. On 1st January, 2015, a Cabinet Resolution was passed to replace the Planning Commission with the newly formed NITI Aayog (National Institution for Transforming India).

GOALS OF FIVE YEAR PLANS

The five year plans have been concerned with the removal of economic backwardness of the country and to make India a developed economy.

- The five years plans have also taken care to ensure that the weaker sections of the population benefit from the economic progress of the country.
- The first five year plan was launched by our first Prime Minister, Pandit Jawaharlal Nehru in the parliament. It was launched for a period starting from 1st April, 1951 and ending on 31st March, 1956. 12th five year Plan of the Government of India (2012 – 17) was India's last Five year Plan. In between these years, some annual plans were also introduced.
- Each five year plan listed the basic Goals of India's development, which served as the guiding principles of Indian planning.
- These basic Goals are:
  1. Growth
  2. Modernisation
  3. Self-reliance
  4. Equity

As all the goals cannot be given equal importance in all the plans, different goals are emphasised in different plans in India. However, the planners have to ensure that, as far as possible, the policies of the plans do not contradict the four goals mentioned above.

Let us now discuss these four goals in detail.

GROWTH

The stagnation during the British rule forced the planners to make Economic Growth as the first and the foremost objective of Indian plans.

- Growth refers to increase in the country's capacity to produce the output of goods and services within the country.
- Growth implies:
    - Either a larger stock of productive capital;
    - Or a larger size of Supporting services like transport and banking;
    - Or an increase in the efficiency of productive capital and services.
- A good indicator of economic growth, in the language of economics, is steady increase in the **Gross Domestic Product (GDP)**.

- GDP refers to market value of all the final goods and services produced in the country during a period of one year. Increase in GDP or availability of goods and services enables people to enjoy a more rich and varied life.
- The GDP of a country is derived from the different sectors (Agricultural sector, Industrial sector and Service sector) of the economy.
- In some countries, growth in agriculture contributes more to the GDP growth, while in some countries, growth in service sector contribute more to GDP growth.
- The contribute of each sector makes up the structural composition of the economy.

Share of Service Sector in GDP increased: By 1990, the share of the service sector was 40.59%, more than that of agriculture or industry. This phenomenon of growing share of the service sector was accelerated in the post 1991 period, which marked the beginning of globalisation in the country.

MODERNISATION

Indian planners have always recognised the need for modernisation of society to raise the standard of living of people. Modernisation includes:

- Adoption of New Technology: Modernisation aims to increase the production of goods and services through use of new technology. For example, a farmer can increase the output on the farm by using new seed varieties instead of using the old ones. Similarly, a factor can increase output by using a new type of machine.
- Change in social outlook: Modernisation also requires change in social outlook, such as gender empowerment or providing equal rights to women. A society will be more civilised and prosperous if it makes use of the talents of women in the work place.

SELF – RELIANCE

The third major objective is to make the economy self-reliant.

- Self-reliance under Indian conditions means overcoming the need of external assistance. In other words, it means to have development through domestic resources.

- To promote economic growth and modernisation, the five year plans stressed on the use of own resources, in order to reduce our dependence on foreign countries.
- The policy of self reliance was considered a necessity because of two reasons:

  - *To reduce foreign dependence:* As India was recently freed from foreign control, it is necessary to reduce our dependence on foreign countries, especially for food. So, stress should be give to attain self – reliance.
  - *To avoid Foreign Interference:* It was feared that dependence on imported food supplies, foreign technology and foreign capital may increase foreign interference in the policies of our country.

EQUITY

The objectives of growth, modernisation and self-reliance, by themselves, may not improve kind of life, which people are living.

- So, it is important to ensure that benefits of economic prosperity are availed by all sections (rich as well as poor) of the economy.
- In addition to the objectives of growth, modernisation and self-reliance equity is also important.
- According to Equity, every Indian should be able to meet his or her basic needs (food, house, education and health care) and inequality in the distribution of wealth should be reduced.
- In short, Equity aims to raise the standard of living of all people and promote social justice.

Let us now discuss how the first seen five year plans (from 1950 to 1990) attempted to attain the four goals and the extent, to which they succeeded in doing so, with reference to 'Agriculture', Industry and 'Trade'.

AGRICULTURE

In the previous chapter, we have learnt that there was neither growth nor equity in the agricultural sector, during the colonial rule.

- At the time of independence, the land tenure system was characterised by intermediaries (like zamindars) who merely collected rent (lagan) from the actual tillers of the soil.

- The low productivity of the agricultural sector forced India to import food from the United States of America.
- The agricultural sector accounted for the largest share of workforce with approximately 70-75 percent. So, agricultural development was focused right from the First Five Year Plan.

FEATURES (OR PROBLEMS) OF AGRICULTURE

Following were some of the main features (or Problems) of Indian agricultural sector between 1950 and 1990:

1. Low Productivity: Indian agricultural sector was known for its low productivity. Lack of knowledge was responsible for stagnation in this sector.

2. Disguised Unemployment: It refers to a state in which more people are engaged in work than are really needed. There was very high incidents of disguised unemployment in the sector during 1950 and 1990.

3. High dependency on Rainfall: Due to poor agricultural technique, farmers depended largely on rainfall. There was minimum growth of this sector in the year that receives the least rainfall.

4. Subsistence Farming: It is the practice of growing crops only for one's own use without any surplus for trade. There was also very high incidents of subsistence farming.

5. Outdated Technology: There were many obsolete technologies and harvesting machines. Harvesting was generally done manually and was very tedious.

6. Conflicts between Tenant and Landlords: Farmers were often a part of a critical contract that bound them to their landlords. Landlords used to extract huge amount of interest from farmers and deprived them of their necessities.

7. Small Land Holdings: Most of the land holdings of the farmers were small. Small land holding is a hindrance in the process of agricultural growth as farming can be carried out by only labour intensive techniques, i.e. use of machines become difficult. Moreover, farmers use their produce (which is obviously less due to small holdings) more for their own use rather for sale in the market.

POLICIES FOR GROWTH OF AGRICULTURE

The measures undertaken to promote the growth in the agricultural sector can be broadly categories as 'Land Reforms' and 'Green Revolution'.

MEASURES TO PROMOTE GROWTH IN AGRICULTURAL SECTOR

Land Reforms
(Involves change in ownership of landholdings through abolition of intermediaries and land ceiling)

Green Revolution
(Refers to large increase in production of food grains due to use of HYV seeds)

LAND REFORMS

Land Reforms primarily refers to change in the ownership of landholdings. Land reform measures have been introduced by various underdeveloped and developing countries, for attaining a rational land distribution pattern and viable farming structure.

- There was a great need for land reforms in a country like India, where majority of its population still depends on agriculture.
- Land reforms were needed to achieve the objective of Equity in agriculture.

ABOLITION OF INTERMEDIARIES

Indian Government took various steps to abolish intermediaries and to make tillers, the owners of land.

- *Aim behind 'Land to the Tiller':* The idea behind this step was that ownership of land would give incentives to the actual tillers to make improvements and to increase output (provided sufficient capital was made available to them). Tenants do not have any incentives to make improvements on land since it is the owner of the land who benefits more from higher output. Ownership of land will enable the tiller to make profit from the increased output.

Just for Reference: The importance of 'Land to the Tiller' can be justified with the following incident that took place in former Soviet Union. The farmers in the former Soviet Union used to be very careless while packing fruits for sale. Quite often, rotten fruits were packed by them along with the fresh fruits in the same box. Every Farmer was aware that the rotten fruits will spoil the fresh fruits if they are packed together. Since farmers did not own any land, they neither enjoyed the profits nor suffered the losses. In the absence of ownership rights, there was no incentive no their part to be efficient.

- The abolition of intermediaries brought 200 lakh tenants into direct contact with the government.
- The ownership rights granted to tenants gave them the incentive to increase output and this contributed to growth in agriculture.
- However, the goal of equity was not fully served by abolition of intermediaries because of following reasons:

    i. In some areas, the former zamindars continued to own large areas of land by making use of some loopholes in the legislation;
    ii. In some cases, tenants were evicted and zamindars claimed to be self-cultivators;
    iii. Even after getting the ownership of land, the poorest of the agricultural labourers did not benefit from land reforms.

Let us now discuss 'Land Ceiling ', which was one of the very important measures towards land reforms in the country.

LAND CEILING

Land Ceiling refers to fixing the specified limit of land, which could be owned by an individual.

- Beyond the specified limit, all lands belongings to a particular person would be taken over by the Government and will be allotted to the landless cultivators and small farmers.
- The purpose of land ceiling was to reduce the concentration of land ownership in few hands.
- Land ceiling helped to promote equity in the agricultural sector.
- However, the land ceiling legislation was challenged by the big landlords. They delayed its implementation. This delay time was used by them to get the land registered in the name of close relatives, thereby escaping from the legislation.

CONCLUSION

Land reforms were successful in Kerala and West Bengal because government of these states were committed to the policy of land reforms. Unfortunately, other states did not have the same level of commitment and vast inequality in landholdings continued.

NEW AGRICULTURAL STRATEGY: GREEN REVOLUTION IN INDIA

The new agricultural strategy was adopted in India during the Third Plan i.e., during 1960s. The traditional agricultural practices followed in India were gradually being replaced by modern technology and agricultural practices. The aim of this strategy was to raise agricultural production and productivity in selected regions of the country through the introduction of modern inputs like fertilizers, credit, marketing facilities, etc.

Green Revolution

At the time of independence, about 75% of the country's population was dependent on agriculture.

- India's agriculture vitally depends on the monsoon and in case of shortage of monsoon, the farmers had to face lot of troubles.
- Moreover, the productivity in the agricultural sector was very low due to use of outdated technology and absence of required infrastructure.

- As a result of intensive and continued efforts of many agricultural scientists, this stagnation in agriculture was permanently broken by the 'Green Revolution'.

Green Revolution refers to the large increase in production of food grains due to high yielding variety (HYV) or miracle seeds especially for wheat and rice. Green Revolution is the spectacular advancement in the field of agriculture.

Dr. Norman E. Borlaug an American agricultural scientist is considered to be the 'Father of the Green Revolution'. He was awarded the Nobel Peace Prize in 1970 for breeding higher-yielding varieties. In India, it was mainly found by M.S. Swaminathan.

HYV SEEDS: MAIN REASON FOR AGRICULTURAL REVOLUTION

Agricultural revolution occurred primarily due to the miracle of new wonder seeds {high yielding varieties (HYV) of seeds}, which raised agricultural yield per acre to incredible heights.

- These seeds can be used in those places where there are adequate facilities for drainage and water supply.
- As compared to other ordinary seeds, these seeds need heavy doses of chemical fertilizers (4 to 10 times more fertilizers) to get the largest possible production.
- So, to derive benefit from HYV Seeds, Indian Farmers need to have:
  - Reliable irrigation facilities; and
  - Financial resources (to purchase fertilisers and pesticides).

Indian Economy experienced the success of Green Revolution in 2 phases:

1. In the First phase (Mid 60s to Mid 70s), the use of HYV seeds was restricted to more affluent states (like Punjab, Andhra Pradesh, Tamil Nadu, etc.) Further, the use of HYV seeds primarily benefited the wheat growing regions only.
2. In the second phase (Mid 70s to mid 80s), the HYV technology spread to a larger number of states and benefited more variety of crops.

IMPORTANT EFFECTS OF GREEN REVOLUTION

The spread of Green Revolution technology enabled India to achieve self-sufficiency in food grains. India was no longer at the mercy of America, or any other nation, for the food requirements.

1. Attaining Marketable Surplus: Green Revolution resulted in Marketable surplus'. Marketable or Marketed surplus refers to that part of agricultural produce which is sold in the market by the farmers after meeting their own consumption requirement.
   - Growth in agricultural output makes a difference to the economy only when large proportion of this increase is sold in the market.
   - Fortunately, a good proportion of rice and wheat produced during the green revolution period was sold by the farmers in the market.

2. Buffer Stock of food Grains: The green revolution enabled the government to procure sufficient amount of food grains to build a stock which could be used in times of food shortage.

3. Benefit to low-income groups: As large proportion of food grains was sold by the farmers in the market, their prices declined relative to other items of consumption. The low – income groups, who spend a large percentage of their income on food, benefited from this decline in relative prices.

RISKS INVOLVED UNDER GREEN REVOLUTION

While the nation had immensely benefited from the green revolution, the technology involved was not free from risks.

i. Risk of Pest Attack: The HYV crops were more prone to attack by pests. So there was a risk that small farmers who adopted this technology could lose everything in a pest attack. However, this risk was considerably reduced by the services rendered by research institutes established by the government.

ii. Risk of Increase in Income Inequalities: There was a risk that costly inputs (HYV seeds, fertilizers, etc.) required under green revolution will increase the disparities between small and big farmers since only the big farmers could afford the required inputs.

However, due to favourable steps taken by the government, these fears did not come true. The government provided loans at a low interest rate to small farmers so that they could also have access to the needed inputs.

Since the small farmers could obtain the required inputs, the output on small farms equalled the output on large farms in the course of time. As a result, the green revolution benefited the small as well as rich farmers.

DEBATE OVER SUBSIDIES TO AGRICULTURE

Subsidy, in context of agriculture, means that the farmers get inputs at prices lower than the market prices. In other words, subsidy is the financial assistance provided by the government to procedures to fulfil its social welfare objectives.

- During the initial phases of green Revolution, new technology was looked upon as being risky by the farmers.
- So, it was necessary for the Government to grant subsidies to provide an incentive for adoption of the new HYV technology.
- However, with the passage of time, there has been debate over the huge amount of subsidies granted by the government.

Let us discuss the points in favour and against the grant of subsidies.

Economists in Favour of Subsidies

1. The government should continue with agricultural subsidies as farming in India continues to be a risky business.
2. Majority of the farmers are very poor and they will not be able to afford the required inputs without the subsidies.
3. Eliminating subsidies will increases the income inequality between rich and poor farmers and will violate the ultimate goal of equity.

In brief, subsidies in India are necessary for poor and small farmers, to enable them to make use of modern agricultural techniques. Necessary steps should be taken to ensure that only the poor farmers enjoy the benefits of subsidies and not the fertiliser industry and big farmers.

Economists against the Subsidies

1. According to some economists, subsidies were granted by the Government to provide an incentive for adoption of the new HYV technology. So, after the wide acceptance of technology, subsidies should be phased out as their purpose has been served.

2. Subsidies do not benefit the poor and small farmers (target group) as benefits of substantial amount of subsidy go to fertiliser industry and prosperous farmers.

Therefore, there is no case for continuing with subsidies as it does not benefit the target group it is a huge burden on the government's finances.

SOME IMPORTANT OBSERVATIONS

1. *Prices as Signals:* Price act as signals about the availability of goods. When a good becomes scarce, its price tends to rise and those who use this good are required to make efficient decisions about its use based on the price. For example, with the outspread of corona virus, sanitizers, infrared thermometers, oximeters, masks, etc. became very costly due to their short supply or scarcity in relation to demand. Similarly, when price of petrol is available. It provides an incentive to use less petrol or look for alternate fuels.

2. *Subsidies may lead to wasteful use of resource:* According to some economists substitute do not allow prices to indicate the supply of a good. Examples:

   i. When electricity is provided at a subsidised rate or free, it will be used wastefully without any concern for its scarcity.
   ii. When water is supplied free to the farmers they they may cultivate water intensive crops, even though the water resources in that region may be scarce. As a result, such cropping pattern will further deplete the already scarce resources. If water is priced to reflect scarcity, farmers will cultivate crops suitable to the region.
   iii. Fertiliser and pesticide subsidies result in overuse of resources which can be harmful to the environment.

So, subsidies provide an incentive for waterful use of resources.

CRITICAL APPRAISAL OF AGRICULTURAL DEVELOPMENT (1950 – 1990)

Indian economy inherited stagnant and backward agricultural sector from the British rule. So, immediately after the independence, Indian Government undertook various measures to improve the condition of agriculture.

- The ‘Land Reform’ measures and green Revolution’ were the greatest achievements of the Indian Government in enhancing the agricultural production and productivity.
- Between 1950 and 1990 there had been substantial increase in the agricultural productivity. Agricultural productivity refers to output per hectare of land. As a result of Green revolution, India became self-sufficient in food production. Land Reforms resulted in abolition of zamindari system.
- The Proportion of GDP between 1950 and 1990 contributed by agriculture declined significantly, but not the population depending on it (67.5% in 1950 to 64.9% by 1990).
- Around 65% of the country’s population continued to be employed in agriculture, even till 1990. Agricultural output could have been grown with much less people working in the sector, but industrial and service sector were unable to absorb the extra people involved in agriculture. The involvement of such a large proportion of the population in agriculture was regarded as the important failure of policies followed during 1950-1990.

INDUSTRIAL DEVELOPMENT

The developing countries (like India) can progress only if they have a good industrial sector. Industry provides employment, which is more stable than the employment in agriculture. Industrilialisation promotes modernisation and overall prosperity. Due to this reason, Five year Plans stressed a lot on the industrial development.

At the time of independence, the variety of industries was very limited. The cotton textile and industries were mostly developed in India. There were only two well-managed iron and steel firms: one in Jamshedpur and the other in Kolkata. So, there was a strong need to expand the industrial base with a variety of industries.

For ‘’ Benefits of Industrialisation’’, refer power Booster.

ROLE OF PUBLIC SECTOR IN INDSUTRIAL DEVELOPMENT

At the time of independence, the big question facing the policy makes was to decide the role of government (public sector) and the private sector in industrial development.

There was a need for a leading role of the Public Sector due to the following reasons:

1. Shortage of Capital with Private Sector: Private entrepreneurs did not have the capital to undertake investment in industrial ventures, required for the development of Indian economy. At the time of independence, Tatas and Birlas were the only well known Private entrepreneurs. As a result, Government had to make industrial investment through Public Sector Undertakings (PSU's)

2. Lack of Incentive for Private Sector: The Indian market was not big enough to encourage private industrialists to undertake major projects, even if they had capital to do so. Due to limited size of the market, there was low level of demand for the industrial goods.

3. Objectives of Social Welfare: The objectives of equity and social welfare of the Government could be achieved only through direct participation of the state in the process of industrialisation.

As a result, state had complete control over those industries, that were vital for the economy. The policies of the private sector had to be complementary to those of the public sector, leading the way.

INDUSTRIAL POLICY RESOLUTION 1956

Industrial policy is a Comprehensive package of policy measures which covers various issues connected with different industrial enterprise of the country.

- Industrial Policy is essential for devising various procedures, principles, rules and regulations for controlling industrial enterprise of the country.
- After the Industrial Policy, 1948, Indian Economy had to face a series of economic and so, on 30th April, 1956, a second Industrial Policy Resolution was adopted in India, which also formed the basis of second five year Plan. The 1956 Policy emphasised the need to expand the Public Sector.

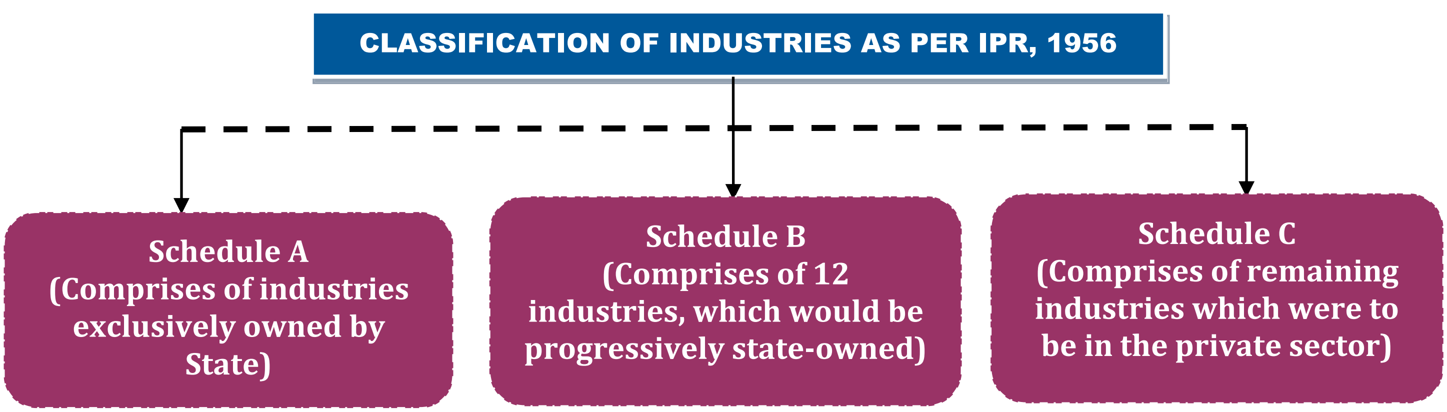
CLASSIFICATION OF INDUSTRIES

According to Industrial Policy Resolution 1956, the industries were reclassified into three categories, viz., Schedule A, Schedule B and Schedule C.

1. Schedule A: This first category comprised industries which would be exclusively owned by the state. In this schedule, 17 industries; aircraft; oil; railways; shipping' etc.

2. Schedule B: In this schedule, 12 industries were placed, which would be progressively state-owned. The state would take the initiative of setting up industries and private sector will supplement efforts of the state. This schedule includes industries like aluminium, other mining industries, machine tools, fertilizers, etc.

3. Schedule C: This schedule consisted of the remaining industries which were to be in the private sector. The state would facilitate and encourage the development of all these industries. These industries were controlled by the state through a system of licenses, enforced under Industries (Development and Regulation) Act, 1951.



INDUSTRIAL LICENSING

An Industrial license is a written permission from the government to an industrial unit to manufacture goods. The industries (Development and Regulation) Act, 1951, empowered the government to issue licenses for:

- Setting up of new industries;
- Expansion of existing ones; and
- Diversification of products.

According to Industrial Licensing

1. No new industry was allowed unless a license is obtained from the government.
2. It was easier to obtain a license if the industrial unit was established in an economically backward area. In addition, such units were given certain concessions, such as tax benefits and electricity at a lower tariff. The purpose of this policy was to promote regional equality.
3. License was needed even if an existing industry wants to expand output or diversify production. License to expand production was given only of the government was convinced that there is a need for larger quantity of goods in the economy.

SMALL-SCALE INDUSTRY (SSI)

In 1955, the Village and Small-scale Industries Committee (Karve Committee) recognised the possibility of using small-scale industries to promote rural development. A 'small-scale industry' is defined with reference to the maximum investment allowed on the assets of a unit. This limit has changed from rupees five lakh in 1950 to present limit of rupees one crore.

IMPORTANT POINTS ABOUT SMALL-SCALE INDUSTRIES

1. Employment Generation: Small-scale industries are more labour intensive, i.e., they use more labour than the large-scale industries and, therefore, they generate more employment. After agriculture, small-scale Industries provide employment to the largest number of people of India.

2. Need for Protection from Big Firms: Small-scale industries cannot compete with the big industrial firms. They can flourish only when they are protected from the large firms. So, various steps were taken by the government for their growth.

- Reservation of Products: Government reserved production of a number of products for the small-scale industry. The criterion for reserving the products depended on the ability of these units to manufacture the goods.

- Various Concessions: Small-scale industries were also given concessions, such as lower excise duty and bank loans at lower interest rates.

FOREIGN TRADE

Foreign trade in India include all imports and exports and from India. India entered into planned development era in 1950's and at that time 'Import' Substitution' was a major element of India's Trade and Industrial Policy. In 1950, India's share in the total world trade was 1.78%.

TRADE POLICY: IMPORT SUBSTITUTION

In order to be self-reliant in vital sectors, India has followed the strategy of replacing many imports by domestic production.

- In the first seven plans, trade was characterised by an inward looking. Trade Strategy. Technically, this strategy is called 'Import Substitution.'
- Import Substitution refers to a policy of replacement or substitution of imports by domestic production.
- For example, instead of importing vehicle made in a foreign country, domestic industries would be encouraged to produce them in India itself.
- The basic aim of the policy was to protect domestic industries from foreign competition.
- The policy of Import Substitution can serve 2 definite objectives:
    i. Savings of precious foreign exchange; and
    ii. Achieving self-reliance.

PROTECTION FROM IMPORTS THROUGH 'TARIFFS AND 'QUOTAS'

Government made use of two ways to protect goods produced in India from imports:

1. Tariffs: Tariffs refer to taxes levied on imported goods. The basic aim for imposing heavy duty on imported goods was to make them more expensive and discourage their use.
2. Quotas: Quota refers to non-tariffs barriers imposed on the quantity of imports and exports. It is fixing the maximum limit on the imports of a commodity by a domestic producer.

The tariff on imported goods and fixation of quotes helped in restricting the level of imports. As a result, the domestic firms could expand without fear of competition from the foreign market.

Reason for Import Substitution

1. The policy of protection (in the form of Import Substitution) is based on the notion that industries of developing countries, like India, are not in a position to complete against the goods produced by more developed economies. With protection, they will be able to complete in the due course of time.
2. Restriction on imports was necessary as there was a risk of drain of foreign exchange reserves on the import of luxury goods.

CRITICAL APPRAISAL OF INDSTRIAL DEVELOPMENT (1950 – 1990)

The achievement of India's industrial sector during the first seven plans are impressive indeed.

1. The proportion of GDP contributed by the industrial sector increased in the period from 11.8% in 1950-51 to 24.6% in 1990-91. This rise in the industry's share of GDP is an important indicator of development. The 6% annual growth rate of the industrial sector during the period is also admirable.
2. Indian Industry was no longer restricted to cotton textiles and jute. It also included engineering goods and a wide range of consumer goods. The industrial sector became well diversified by 1990, largely due to the public sector.

3. The promotion of small-scale industries gave opportunities to people with small capital to get into business. New investment opportunities helped in generating more employment. It promoted growth with equity.
4. Protection from foreign Competition (through Import Substitution) enabled the development of indigenous industries in the areas of electronics and automobile sectors, which otherwise could not have developed. However, this protection had two drawbacks:

   i. Inward Looking Trade Strategy: Our policies were 'inward oriented' and so we failed to develop a strong export sector.

   ii. Lack of Competition: Due to restrictions on imports, some domestic procedures made no, sincere efforts to improve the quality of their goods and it forced the Indian consumers to purchase, whatever is produced by them. The domestic industry failed to achieve international standards of product quality.

   According to some economists, we should protect our producers from foreign competition as long as the rich nations continue to do so.

5. Licensing Policy helped the government to monitor and control the industrial production. However, excessive regulation by the government created two difficulties:

   i. Misuse: It was misused by industrial houses. Some big industrialists would get a license, not for starting a new firm, but to prevent competitors from starting new firms.
   ii. Time Consuming: The cumbersome and complex procedure for obtaining license was very time consuming. A lot of time was spent by industrialists in trying to obtain a license.

6. Public sector made a remarkable contribution by creating a strong industrial base, developing infrastructure and promoting development of backward areas.

- However, the public sector continued to monopolise (that too ineffectively) in certain non-essential areas, which could be well handled by the private sector. For example, telecommunication, hotel industry, production of goods (like Modern Bread).

- As a result, precious funds of public sector channelised into areas, where private sector could have been easily engaged.
- Many public sector firms also incurred huge losses but continued to function because of difficulty in closing a government undertaking.
- The monopoly of public sector in such non-essential areas was criticized by many scholars. According to them, the role of public sector should be limited to strategic areas (like national defence) and private sector should be given the opportunity for other non-essential areas.

According to some economists, public sector in not meant for earning profits but to promote the welfare of the nation. So, they should be evaluated on the basis of their contribution to welfare of the people and not on the profits they earn.

CONCLUSION

The progress of the Indian economy in the three sectors can be summarised as under:

In Agriculture Sector:

- India became self-sufficient in food production due to the green revolution.
- Land reforms resulted in abolition of zamindari system.

In Industrial Sector:

- The industries became far more diversified compared to the situation at independence. However, excessive government regulation prevented their growth.
- Many economists were dissatisfied with the performance of public sector enterprises.

In Trade Sector:

- Our policies were 'inward oriented' and so we failed to develop a strong export sector.
- The domestic producers were protected against foreign competition in order to gain self-reliance. However, this did not give them the incentive to improve the quality of goods that they produced.

The need for reform of economic policy was widely felt in the context of changing global economic scenario. So, the New Economic policy (NEP) was initiated in 1991, to make our economy more efficient. This is the subject of the next chapter.

UNIT – 2

CRISIS OF 1991 FORCED INDIA FOR FINANCIAL HELP FROM IMF AND WORLD BANK

To manage the economic crisis of 1991, Indian Government approached for loan from:

- International Bank for Restruction and Development (IBRD) popularly known as World Bank (to facilitate lending for reconstruction and development); and
- International Monetary fund (IMF) (to avoid short-term loans to solve balance of payments problem).

India availed $ 7 billion loan from these agencies as loan. Dr. Manmohan Singh was the Indian Finance Minister in 1991 and he was greatly acknowledged for his capabilities to steer away the economic crisis looming large on the Indian Economy.

For availing the loan, these international agencies expected India to liberalise and open up the economy by:

- Removing restriction on the private sector;
- Reducing the role of the government in many areas; and
- Removing trade restrictions.

India agreed to the conditions of World Bank and IMF and announced the New Economic Policy.

THE NEW ECONOMIC POLICY

The New Economic Policy (NEP) was announced in July 1991. It consisted of wide range of economic reforms. The main aim of the policy was to create a more competitive environment in the economy and remove the barriers to entry and growth of firms.

The New Economic policy can be broadly classified into two kinds of measures:

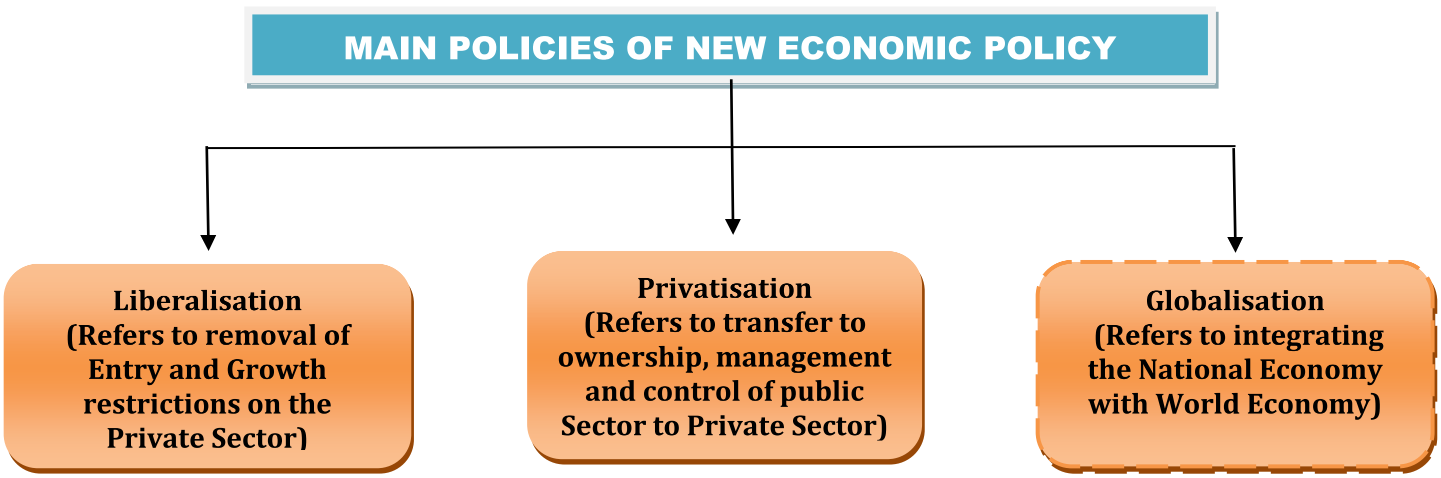
1. Stabilisation Measures: They refer to short-term measures which aim at:
   i. Correcting weaknesses of the balance of payments by maintaining sufficient foreign exchange reserves; and
   ii. Controlling inflation by keeping the rising prices under control.
2. Structural Reform Measures: They refer to long-term measures which aim at:
   i. Improving the efficiency of the economy; and
   ii. Increasing international competitiveness by removing the rigidities in various segments of the Indian economy.

MAIN POLICIES OF NEW ECONOMIC POLICY

The government initiated a variety of policies which fall under three heads:

1) Liberalisation
2) Privatisation
3) Globalisation

Liberalisation, Privatisation and Globalisation or 'LPG' are the supporting pillars, on which the structure of new economic policy of our Government has been erected and implemented since 1991.



Let us discuss them one by one.

Liberalisation

Prior to 1991, there were large number of government restrictions in India in the areas of licensing, import and export trade, dealings in foreign exchange, etc. In july 1991, a package of economic reforms was announced, which marked the beginning of process of 'Liberalisation' in India. Liberalisation means removal of entry and growth restrictions on the private sector.

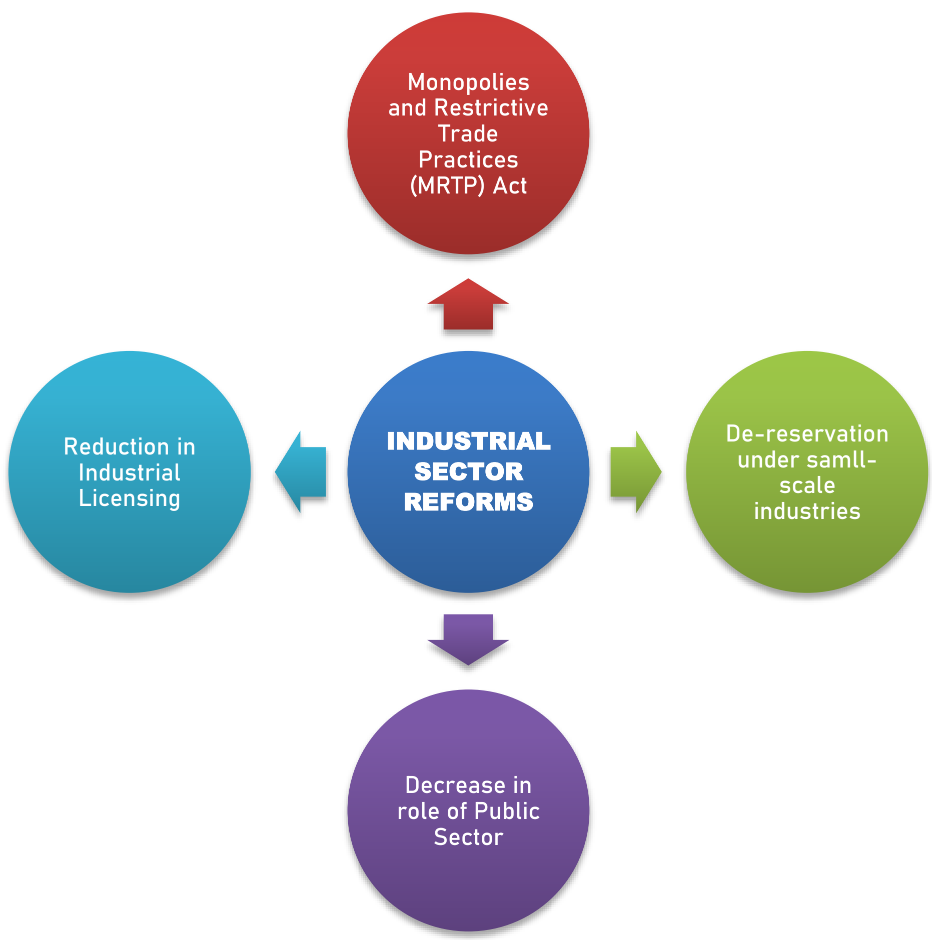
- Liberalisation involves deregulation and reduction of government controls and greater autonomy (freedom) of private investment, to make economy more competitive.
- Under this process, business is given free hand and is allowed to run on commercial lines.
- The purpose of liberalisation was:
  - To unlock the economic potential of the country by encouraging private sector and multinational corporations to invest and expand; and

    - To introduce much more competition into the economy and creating incentives for increasing efficiency of operations.
- The economic reforms taken by the Government under liberalisation include the following:
    i. Industrial Sector Reforms
    ii. Financial Sector Reforms
    iii. Tax Reforms
    iv. Foreign Exchange Reforms
    v. Trade and Investment Policy Reforms

Let us now discuss each reform in detail.

Industrial Sector Reforms

In order to make necessary reforms in the industrial sector, the Government introduced its new industrial policy on july 24, 1991. The various measures under industrial policy reforms include:



1. Reduction in Industrial Licensing: The new policy abolished industrial licensing for all the projects, except for 18 industries. This number was further reduced to 5 industries. They are: (i) Distillation and brewing of alcoholic drinks; (ii) Cigars and cigarettes of tobacco and manufactured tobacco substitutes; (iii) Electronic Aerospace and defence equipments; (iv) Industrial explosives; (v) Specified Hazardous chemicals.

- No licences were needed (i) To set up new units; or (ii) Expand or diversify the existing line of manufacture.
- However, compulsory licensing is required for the above mentioned 5 industries on account of environmental, safety and strategic considerations.

2. Decrease in role of Public Sector: One of the striking features was the substantive reduction in the role of the public sector in the future industrial development of the country. Under from 17 to 8, which was further reduced to just three (in 2010-11) namely Atomic Energy, Railways and Defence Equipments.

3. De-reservation under small-scale industries: Many goods produced by small scale industries have now been de-reserved.
    - The investment ceiling on plant and machinery for small undertakings enhanced to rupees one crore.
    - In many industries, the market was allowed to determine the prices through forces of the market (and not by directive policy of the government).

4. Monopolies and Restrictive Trade Practices (MRTP) Act: With the introduction of liberalisation and expansion schemes, the requirement for large companies, to seek prior approval for expansion, establishment of new undertakings, merger, amalgamations, etc. were eliminated. MRTP Act has been replaced by Competition Act, 2002, which is more liberal. The Competition Act, 2002 was amended by the Competition (Amendment) Act, 2007 and again by the Competition (Amendment) Act, 2009.

Financial Sector Reforms

Financial sector includes financial institutions like commercial banks, investment banks, stock exchange operations and foreign exchange market. The financial sector in India is controlled by the Central Bank – Reserve Bank of India (RBI). RBI is known as the apex (supreme) body as it occupies the top most position in the monetary and banking system of the country. RBI decides the amount of money (i.e. deposits) that the banks can keep with themselves, fixes interest rates and nature of lending to various sectors.

The reforms introduced under financial sector are:

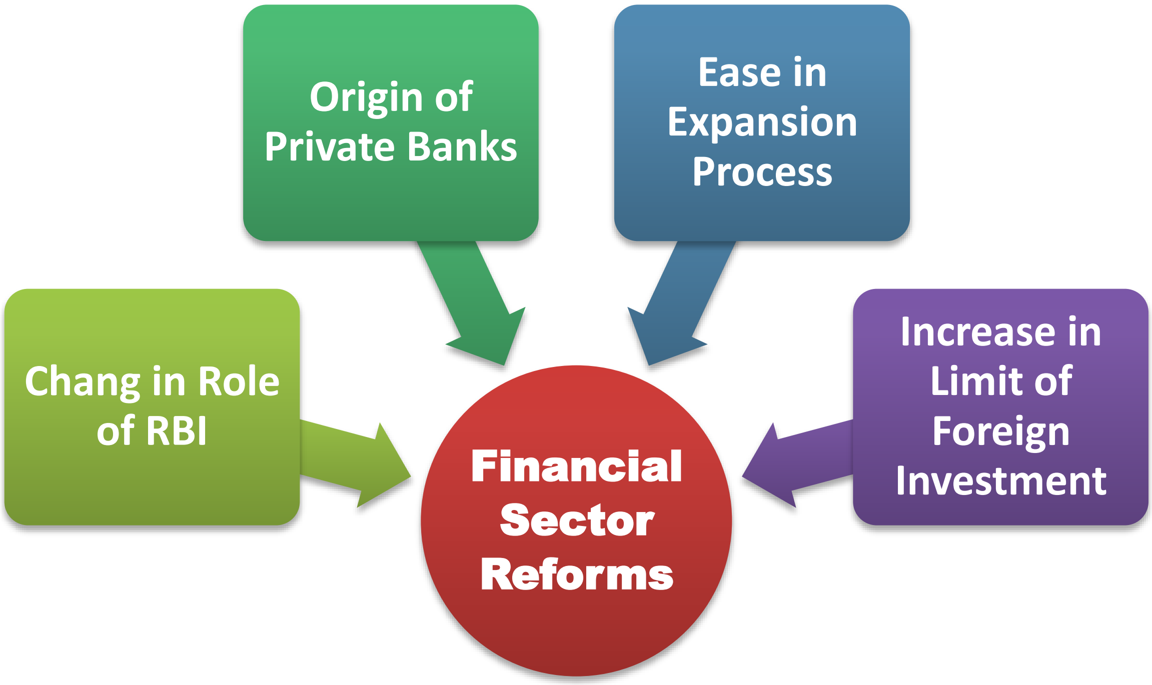
1. Change in Role of RBI: The role of RBI was reduced from regulator to facilitator of financial sector. As a result, financial sector was allowed to take decisions on many matters, without consulting the RBI.

   As a regulator (prior to liberalisation), RBI used to fix interest rate structure for the commercial Banks, After changing the role as a facilitator (post-liberalisation), RBI now facilitates the free market forces to act accordingly. In the post liberalisation era, greater autonomy has been ensured for financial institutions for their functioning.

2. Origin of Private Banks: The reform policies led to the establishment of private sector banks, Indian as well as foreign. For example, Indian banks like ICICI and foreign banks like HSBC Increased the competition and benefitted the consumers through lower interest rates and better services.

3. Increase in limit of Foreign investment: The limit of foreign investment in banks was raised to around 74%. Foreign Institutional Investors (FII) such as merchant bankers, mutual funds and pension funds were now allowed to invest in Indian Financial markets.
   Though banks have been given permission to generate resources from India and abroad, certain aspects have been retained with the RBI to safeguards the interests of the account-holders and the nation.

4. Ease in Expansion Process: Banks were given freedom to set up new branches (after fulfilment of certain conditions) without the approval of the RBI.



Tax Reforms

Tax reforms refer to reforms in government's taxation and public expenditure policies, which are collectively known as its 'Fiscal Policy'. Taxes are of two types:

- Direct Taxes consist of taxes on incomes of individuals as well as profits of business enterprises. For example, Income tax (taxes on individual incomes) and Corporate tax (taxes on profits of Companies).
- Indirect Taxes refer to those taxes which affect the income and property of persons through their consumption expenditure. Indirect taxes are generally imposed on goods and services.
  For example, Goods and services Tax (GST).

The major Tax Reforms made are:

1. Rationalisation of Direct Taxes: Since 1991, there has been a continuous reduction income and corporate tax as high tax rates were an important reason for tax evasion. It is now widely accepted that moderate rates of income tax encourage savings and voluntary disclosure.
2. Reforms in Indirect taxes: Considerable reform have been made in indirect taxes to facilitate establishment of common national market for goods and commodities.
3. Simplification of Process: In order to encourage better compliances on the part of taxpayers, many procedures have been simplified.

The Goods and service Tax Act was passed in the Parliament on 29th March, 2017 to simplify and introduce a unified indirect tax system in India. The Act came into effect on 1st july 2017. This is expected to generate additional revenue tax evasion and create ‘one nation, one tax and one marker.

FOREIGN EXCHNAGE REFORMS

The important reforms made in the foreign exchange market are:

1. Devaluation of Rupee: Devaluation refers to deliberate reduction in the value of domestic currency vis-à-vis any foreign currency by the government of a country. To overcome Balance of payments crisis in 1991, the rupee was devalued against foreign currencies. This led to an increase in the inflow of foreign exchange.
2. Market Determination of Exchange Rate: The Government allowed rupee value to be free from its control. As a result, market forces of demand and supply determine the exchange value of the Indian rupee in terms of foreign currency.

Trade and Investment Policy Reforms

Before 1991, a lot of restrictions (high tariffs and quotes) were imposed on imports to protect the domestic industries. However, this protection reduced the efficiency and competitiveness of domestic industries and led to their slow growth. So, the reforms in the trade and investment policy were initiated.

- To increase the international competitiveness of industrial production.
- To promote foreign investments and technology into the economy.
- To promote efficiency of local industries and adoption of modern technologies.

The important trade and investment policy reforms include:

1. Removal of Quantitative restrictions on Imports and Exports: Under the New Economic policy, quantitative restrictions on imports and exports were greatly reduced. For example, quantitative restrictions on imports of manufactured consumer goods and agricultural products were fully removed from April 2001.

2. Removal of Export Duties: Export duties were removed to increase the competitive position of Indian goods in the international markets.

3. Reduction in Import Duties: Import duties were considerably reduced, which improved the competitiveness of domestic industries as it enabled them to import raw materials at better prices.

4. Relaxation in Import Licensing System: The Import Licensing was abolished, except in case of hazardous and environmentally sensitive industries. This encouraged domestic industries to import raw materials at better prices, which raised their efficiency and made them more competitive.

Another important feature of new economic policy was the promotion of the policy of ''Privatisation''.

PRIVATISATION

Privatisation means transfer of ownership, management and control of public sector enterprises to the entrepreneurs in the private sector.

Privatisation implies greater role of the private sector in the economic activities of the country over the years, Indian Government has diluted its stake in several public enterprises, including IPCL, IBP, Maruti Udyog, etc.

Privatisation can be done in two ways:

1. Transfer of ownership and management of public sector companies from the government to the Private Sector;
2. Privatisation of the public sector undertakings (PSU) by selling off part of the equity of PSUs to the public. This process is known as disinvestment.

The purpose of privatisation was mainly to improve financial disciple and facilitate modernisation. It was also believed that private capital and managerial capabilities will help in improving performance of the PSUs.

For ''Arguments in favour of Privatisation'' and ''Arguments Against Privatisation''. refer power Booster section.

GLOBALISATION

Globalisation means integrating the national economy with the world economy through removal of barriers on international trade and capital movements.

- Globalisation is generally understood to mean integration of the economy of the country with the world economy.
- However, it is a complex phenomenon. It is an outcome of the set of various policies that aim to transform the would towards greater interdependence and integration.

- It involves creation of networks and activities transcending economic, social and geographical boundaries. In short, globalisation aims to create a borderless world.

Change made by the Globalisation of the Indian Economy

1. The New Economic Policy prepared a specified list of high technology and high investment priority industries, in which automatic permission will be available for foreign direct investment up to 51 per cent of foreign equity.
2. In respect of foreign technology agreements, automatic permission is provided in high priority industry upto a sum of rupees 1 crore. No permission is now required for hiring foreign technicians or for testing indigenously developed technology abroad.
3. In order to make international adjustment of Indian currency, rupee was devalued in July 1991 by nearly 20 per cent. It stimulated exports, discouraged imports and raised the influx of foreign capital.
4. To integrate Indian economy with world, the Union Budget 1992-93 made Indian rupee partially convertible and then the rupee was made fully convertible in 1993-94 budget.
5. A new five year export-import policy (1992-97) was announced by the Government to establish the framework of globalisation of India's foreign trade. The policy removed all restrictions and controls on the external trade and allowed market forces to play a greater role in respect of exports and imports.
6. In order to bring the Indian economy within the ambit of global competition, the government has modified the customs duty to a considerable extent. Accordingly, the peak rate to customs duty has been reduced from 250 per cent to 10per cent in 2007-2008 budget.

POSITIVE AND NEGATIVE TRAITS OF GLOBALISTAION

The process of globalisation through liberalisation and privatisation policies, has produced positive as well as negative results, both for India and other countries.

In Favour of Globalisation

Globalisation resulted in:

- Greater access to global markets;
- Advanced technology ;
- Better future prospects for large industries of developing countries to become important players in the international arena.

- Better prospects for skilled people across the globe to increase their earnings by utilising their skills.

Against Globalisation

Globalisation has been criticized by some scholars because according to them:

- Benefits of globalisation accrue more to developed countries as they are able to expand their markets in other countries.
- Globalisation compromises the welfare and identify of people belonging to poor countries.
- Market-driven globalisation increases the economic disparities among nations and people.
- As a result of Globalisation, MNC_s have gained strong position in the developing countries, due to which domestic companies are forced to face stiff competition.

Outsourcing

Outsourcing refers to contracting out some of its activities to a third party which were earlier performed by the organisation. For example, many companies have started outsourcing security service to outside agencies on a contractual basis.

- Outsourcing is one of the important outcomes of the globalisation process. Outsourcing is emerging as a major activity in industrial and service sectors.
- It has intensified in recent times because of the growth of fast modes of communication, particularly the growth of Information Technology (IT).
- With the help of modern telecommunication links, the text, voice and visual data in respect of these services is digitised and transmitted in real time over continents and national boundaries.
- India has become a favourable destination of outsourcing for most of the MNC's because of:
    - Availability of Skilled Manpower: India has vast skilled manpower which enhances the faith of MNCs for investment in India.
    - Favourable Government Policies: MNCs get various types of lucrative offers from the Indian Government such as tax holidays, tax concessions, etc.
    - Low Wage Rates and availability of cheap labour in India for skilled work.
    - Considerable growth of Indian IT industry, which has proved its competitive strength in the world.

For example, Indian Business Process Outsourcing (BPO) companies are already gaining prominence and earning precious foreign exchange.

WORLD TRADE ORGANISATION (WTO)

Origin of World Trade organisation (WTO)

Prior to WTO, General Agreement on Trade and Tariff (GATT) was established as global trade organisation, in 1948 with 23 countries. GATT was set up to administer all multilateral trade agreements by providing equal opportunities to all countries in the international market. WTO was founded in 1995 as the successor organisation to the GATT.

- The WTO agreements cover trade in goods as well as services, to facilitate international trade.
- At present, there are 164 member countries of WTO and the all the member are required to abide by laws and policies framed under WTO rules.
- As an important member of WTO, India has been in the forefront of framing fair global rules, regulations and advocating the interests of developing world.
- India has kept its commitments made to the WTO. India has taken reasonable steps to liberalise trade by removing quantitative restrictions on imports and reducing tariff rates.
- Some Major Functions of WTO:
    i. To facilitate international trade (both bilateral and multi-lateral trade)through removal of tariffs as well as non-tariff barriers;
    ii. To establish a rule-based trading regime, in which nations cannot place arbitrary restrictions on trade;
    iii. To enlarge production and trade of services;
    iv. To ensure optimum utilisation of world resources; and
    v. To protect the environment.

Should India be a member of WTO?

Some scholars are of the view that there is no use for a developing country like India to be a member of the WTO. According to them:

i. Major volume of international trade occurs among the developed nations; and
ii. Developing countries are being cheated as they are forced to open up their markets for developed countries and are not allowed access to markets of developed countries.

AN APPRAISAL OR LPG POLICIES (ECONOMIC REFORMS)

Economic reforms created mixed reactions at different levels. Let us discuss some of the positive and negative aspects of economic reforms.

ARGUMENTS IN FAVOUR OF ECONOMIC REFORMS

The following are some of the important arguments advanced in favour of economic reforms:

1. Increase in rate of Economic Growth: The growth in GDP was 5.6% during 1980-91 as compared to growth rate of 6.7% in 2017-18. In the second quarter of 2021, (i.e. july to September, 2021) GDP growth was recorded at an impressive 8.4%
    - During the reform period, the growth of agriculture has declined and industrial sector reported fluctuation, whereas, growth of service sector has gone up. This indicates
    - During 2012-15, there has been a setback in the growth rates of different sectors. Agriculture recorded a high growth rate of 10.3% in 2014-15. The industrial sector witnessed a steep decline during 2012-13, but began to show a positive growth thereafter.
2. Inflow of Foreign Investment: The opening up of the economy has led to the rapid increase in foreign direct investment (FDI). The foreign investment (FDI and foreign institutional investment) increased from about US $ 100 million in 1990 – 91 to US $ 30 billion in 2017-18. With launch of 'Make in India initiative in September 2014, Foreign Direct Investment (FDI) Policy was further liberalized. Due to this reason, FDI Inflow in India increased by 48%
3. Rise in Foreign Exchange Reserves: There has been an increase in the foreign exchange Reserves from about US $ 6 billion in 1990-91 to about US $ 443 billion in 2018-19, which increased to US $ 637.687 billion (as on 26th November, 2021 as per RBI). India is one of the largest foreign exchange reserve holders in the world.
4. Rise in Exports: Since 1991, India experienced considerable increase in exports of auto parts, pharmaceutical goods, engineering goods, IT Software and textiles.
5. Control on Inflation: Increase in production, tax reforms and other reforms helped in controlling the inflation. The annual rate of inflation reduced from the peak level of 17% in 1991 to around 5.48% in 2015-16 for 2022-23, RBI estimates Indicate that inflation will move in a range of 4.5-5.2 per cent.

6. Increase in role of Private Sector: Abolition of licensing system and removal of restrictions on entry of the private sector, in areas earlier reserved for the public sector, have enlarged the area of operation of the private sector.

Criticism of Economic Reforms

Critics have raised a series of criticism against the New Economic Reforms, especially in the areas of employment, agriculture, industry, infrastructure development and fiscal management.

1. Growing Unemployment: Though the GDP growth rate has increased in the reform period, but such growth failed to generate sufficient employment opportunities in the country.
2. Neglect of Agriculture: The new economic policy has neglected the agricultural sector as compared to industry, trade and services sector.
   i. Reduction of Public investment: Public investment in agriculture sector, especially in infrastructure, which includes irrigation, power, roads market linkage and research and extension (which played a crucial role in the Green Revolution), has been reduced.
   ii. Removal of subsidy: Removal of fertilizer subsidy increased the cost of production, which adversely affected the small and marginal farmers.
   iii. Liberalisation and reduction in import duties: This sector has been experiencing a number of policy changes such as: (a) Reduction in import duties on agricultural products; (b) Removal of minimum support price; and (c) Lifting of quantitative restrictions on agricultural products. All these policies adversely affected the Indian Farmers as they now have to face increased international competition.
   iv. Shift towards cash crops: Due to Export-oriented policy strategies in agriculture, the production shifted from food grains to cash crops for the export market. It led to rise in the prices of food grains.
3. Low level of Industrial Growth: Industries growth recorded a slowdown due to the following reasons:
   i. Cheaper Imported Goods: Due to globalisation, there was a greater flow of goods and capital from developed countries and as a result, domestic industries were exposed to imported goods. Cheaper imports replaced the demand for domestic goods and domestic manufacturers started facing competition from imports. For example, Cheaper Chinese goods a pose a big threat to Indian manufactures.
   ii. Lack of infrastructure facilities: The infrastructure facilities, including power supply, have remained inadequate due to lack of investment.

iii. Non-Tariff Barriers by Developed countries: All quota restrictions on exports of textiles and clothing have been removed from India. But some developed countries, like USA have not removed their quota restrictions on import of textiles from India.

4. Ineffective Disinvestment Policy: The government has always fixed a target for disinvestment of Public Sector Enterprises (PSEs). For instance, in 1991-92, it was targeted to mobilise Rs. 2,500 crore through disinvestment. The government was able to mobilise Rs. 3,040 crore more than the target. In 2017-18, the target was Rs. 1,00,000 crore, whereas, the achievement was about Rs. 1,00,057 crore.
   However, according to some scholars, the disinvestment policy of government was not successful because:
   - The assets of PSEs were undervalued and sold to the private sector.
   - Moreover, such proceeds from disinvestment were used to compensate shortage of government revenues rather than using it for the development of PSEs and building social infrastructure in the country.
5. Ineffective Tax Policy: The tax reduction in the reform period was done to generate larger revenue and to curb tax evasion. But, it did not result in increase in tax revenue for the government.
   - Tariff reduction decreased the scope for raising revenue through customs duties.
   - Tax incentives provided to foreign investors to attract foreign investment further reduced the scope for raising tax revenues.
6. Spread of Consumerism: The new policy has been encouraging a dangerous trend of consumerism by encouraging the production of luxuries and items of superior consumption.
7. Unbalanced Growth: Growth has been concentrated only in some select areas in the service sector, such as telecommunication, information technology, finance, entertainment, travel and hospitality services, real estate and trade, rather vital sector, such as agriculture and industry, which provide livelihood to millions of people in the country.